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DEPARTMENT OF THE AIR FORCE
HEADQUARTERS UNITED STATES AIR FORCE
WASHINGTON 25, D.C.

J.M.
DPA 0179-59
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REPLY TO:

HQ Eastern District
Auditor General
Comptroller, USAF
Liaison Office
Washington, D.C.

4 December 1958

SUBJECT: Advisory Report on Evaluation of Proposed Rates
Itek Corporation
Boston, Massachusetts
Subcontract Proposal with Prime Contractor
Period: 1 May 1958 to 31 October 1959

TO : Contracting Officer

REF : Verbal request of J.M. on 25 Nov. 58

1. An evaluation of the Subcontractor's proposal, dated 17 November 1958, in the amount of \$4,641,832, was made for the purpose of determining acceptability of the proposed rates.

2. This proposal superseded the earlier proposal for approximately \$6,000,000.

3. The scope of our examination was as follows:

a. All calculations contained in the proposal were verified.

b. All rates, including the following, were verified:

- (1) Direct Engineering Labor Rates.
- (2) Fabrication Labor Rate.
- (3) Engineering Overhead Rates.
- (4) Fabrication Overhead Rates.
- (5) General and Administrative Rate.

c. Actual Engineering and Fabrication Labor costs incurred thru 31 August 1958, as shown in Schedule I, and totalling \$91,699 were verified. We also determined the propriety of the overhead claimed on this labor, in the amount of \$97,149. However, no attempt was made at this time to audit the individual items of experienced cost.

d. We also reviewed the estimated amount of \$108,835. shown for travel expense in Schedule I.

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e. The proposal of the Long Island Second Tier Subcontractor, shown on line 24 of Schedule I, amounting to \$2,410,144, was the subject of another audit report on evaluation of proposed rates recently issued to the Contracting Officer.

4. We did not review the following elements, since they were considered to be items requiring technical determination:

- a. Labor hours.
- b. Estimated Material and other Direct Costs exclusive of Travel.
- c. Allowance for Fixed Fee.

5. Computation of Labor Rates: The Subcontractor utilized average labor rates for each labor classification, computed as follows:

- a. For averaging purposes, all labor was divided into twenty classes (15 Engineering and 5 Fabrication).
- b. Each of the above classes was subdivided into one or more sub-classifications.
- c. Actual average rates for each sub-classification as of 9 September 1958 were arrived at by listing of the Payroll Earnings Records.
- d. To these rates was added a 10% factor for merit and general increases.
- e. The average sub-class rates produced in d. above were then again averaged together to obtain the primary classification rates, which are contained in the Subcontractor's cost proposal.

6. Comments on Subcontractor's Method of Computing Labor Rates:

a. The Project Auditor pointed out to the Subcontractor that, thru the method outlined above where sub-class average rates are again averaged to obtain primary class rates, the primary class rates which are produced tend to be slightly higher than if a straight average of all personnel in the primary class were obtained. The reason for this is that the higher rate sub-classes only comprise one or two individuals, whereas the lower rate sub-classes comprise many individuals.

b. The Subcontractor states that the method used is consistent with past practice and has been accepted in prior Government contract negotiations.

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c. The Auditor has tentatively accepted the method utilized by the Subcontractor, subject to the concurrence of the Contracting Officer.

7. Overhead Rates:

a. The Corporation's fiscal year ends 30 September.

b. As of 31 May, Vectron, Inc. (Waltham Plant) was merged into Itek Corporation.

c. At the present time separate Engineering and Fabrication Overhead rates are negotiated with the Government for both the Boston and Waltham Plants.

d. Actual book rates for the short fiscal year 1 June 1958 to 30 September 1958 were as follows:

	<u>Boston</u>	<u>Waltham</u>	<u>Combined</u>
Engineering	102.34%	73.57%	
Fabrication	106.42%	145.38%	
G & A			6.098%

e. The Subcontractor utilized the following rates for both actual costs incurred thru 31 August 1958 and the run-out portion of the subcontract proposal:

	<u>Combined Rate</u>
Engineering	100%
Fabrication	150%
G & A	10%

f. The Subcontractor states that there are no overhead projections in existence covering the fiscal year 1 October 1958 thru 30 September 1959. Therefore, utilizing the most recent recorded experience the auditor is accepting the following rates for purposes of this proposal:

(1) Actual costs thru 8/31/58:

	<u>Boston</u>	<u>Waltham</u>	<u>Combined</u>
Engineering	102%	74%	
Fabrication	106%	145%	
G & A			6%

(2) Run-out portion of contract:

	<u>Combined</u>
Engineering (most of effort at Boston)	100%
Fabrication (most of effort at Waltham)	145%

G & A

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8. Travel Expense:

a. Travel Expense shown in Schedule I includes the following items:

(1) Subsistence for 1,314 man days of technical support computed at \$30 per diem for a total of \$39,420. Since Air Force Regulations preclude reimbursement in excess of \$15 Per Diem unless specifically approved by the Contracting Officer, we have not accepted the entire amount proposed.

(2) Per Diem for Field Servicemen traveling away from their temporary duty stations (Room rental at Gov't BOQ computed at \$12 per week) for 40 man weeks, or a total of \$480. This is in addition to the per diem rates paid to the employee and his family for relocating on a temporary duty basis, and essentially represents "per diem on per diem". Although we have not considered this cost as non-acceptable, it is referred to the Contracting Officer for further consideration at the time of negotiations.

(3) Anticipated cost of moving household goods of two Field Servicemen to their temporary duty stations, \$3,000. This cost may never accrue since the employees may not wish to move their household effects (TDY period to last for approximately 10 months). The Corporation states this is their consistent policy where long temporary duty periods are involved, in order to avoid inconvenience to the employee. Accordingly, this item is also referred to the Contracting Officer for further consideration.

b. Other elements comprising the travel expense category, including estimated transportation costs and the number of estimated trips and/or man days, appear to be reasonably computed.

9. Offer made by the Subcontractor to Reduce the Proposal by \$400,000:

a. We were informed by the Subcontractor that since the time this proposal was submitted, discussions between the Prime Contractor and First and Second Tier Subcontractors have resulted in a request by the Prime Contractor that, due to a lack of funds, this proposal be substantially reduced.

b. The Subcontractor tentatively proposes a \$400,000 reduction be made, thus reducing the \$4,600,000 total to \$4,200,000. The proposed reduction would be shared \$200,000 by the subcontractor and \$200,000 by the Second Tier Subcontractor.

c. To date the proposed reduction has not as yet been accepted by the Second Tier Subcontractor, or by the Prime Contractor, who feels that the reduction should be greater.

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10. Results of Examination:

a. Questionable Items Included in Proposal - \$207,600:

(1) Costs not Accepted - Schedule I - \$203,190: Represents overhead rate differences (See Par. 7) and Travel mentioned in Par. 8.a.(1), plus applicable Fixed Fee.

(2) Costs not Accepted - Schedule II - \$295: Represents G & A rate difference (See Par. 7) plus applicable Fixed Fee.

(3) Costs for Further Consideration - Schedule III - \$4,115: Represents Travel items mentioned in Pars. 8.a. (2) and (3), plus applicable G & A and Fixed Fee.

b. Subject to the above questionable items, and comments contained in Par 6 above, the labor rates, overhead rates, estimated travel expense and engineering and fabrication labor costs incurred to date, are considered reasonable for purposes of this procurement. See Par. 3.e. with respect to the estimated costs of the Long Island Second Tier Subcontractor.

11. Subcontractor's Reaction to Auditor's Findings:

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a. The questionable items summarized in Par. 10.a. were discussed with [redacted] Contract Administrator, on 2 December 1958. The Subcontractor's position is as follows:

(1) Concurs: With \$6,356 overhead rate differences on costs incurred to date (Schedule I).

(2) Does not Concur: With all other items. They feel that the 100% engineering rate claimed for the run-out portion of the contract will be insufficient and this is an offset against the rate of 150% claimed for Fabrication. They also feel that the 6% G & A rate accepted by the auditor is too low.

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b. Although the Subcontractor disagrees in principle with most of the questionable items, [redacted] stated that they would accept all of these item (\$207,600) in accordance with their offer to reduce their own portion of the proposal by \$200,000 (Par 9.b.) providing this is accepted by the Prime Contractor. However, they are not agreeable to these reductions in addition to the \$200,000 proposed reduction, which would result in a \$600,000 total reduction (\$400,000 of their own work plus \$200,000 for the Sub-Subcontractor).

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12. The proposal contains a slight typographical error on
Schedule IV. The final cumulative total should be \$4,641,832 instead
of \$4,641,032. See Schedule III for reference to the correct total.

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Liaison Officer
Eastern District
Auditor General

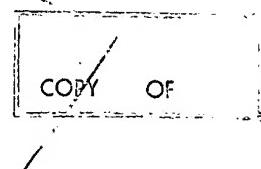
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Schedule I
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Itek Corporation
 Boston, Mass.
 Subcontract Proposal to Prime Contractor
 Costs Not Accepted - Schedule I of Cost Proposal

	<u>Base</u>	<u>Acceptable Rate</u>	<u>Acceptable</u>	<u>Amount Claimed</u>	<u>Difference</u>
1. Actual Costs thru 31 August 58:					
<u>Engineering Overhead:</u>					
Boston	\$66,028	102%	\$67,349		
Waltham	<u>14,771</u>	74%	<u>10,931</u>		
Total	<u>\$80,799</u>		<u>\$78,280</u>		
				\$80,799(A)	\$ 2,499
<u>Fabrication Overhead:</u>					
Boston	\$ 8,494	106%	\$ 9,004		
Waltham	<u>2,406</u>	145%	<u>3,489</u>		
Total	<u>\$10,900</u>		<u>\$12,493</u>		
				\$16,350(B)	\$ 3,857
					\$ 6,356
2. Fabrication Overhead:					
Labor - Line 15	\$23,960	145%	\$34,742		
				\$35,940(B)	\$ 1,198
3. Travel:					
Phase I:					
Per diem @ \$30 for 1,314 M/Days				\$39,420	
@ \$15			\$19,710		
Add: Additional estimated auto rental costs includable in subsistence					
			1,080		
			<u>\$20,790</u>		
					\$18,630
Sub Total					\$26,184
4. G & A:					
10% of sub-total (claimed rate)					2,618
G&A on approved base:					
Per proposal \$4,034,959					
Less: Questioned					
above (26,184)					
Schedule III (3,480)					
Approved Base \$4,005,295(D)	6%		\$240,318		
Sub Total				\$400,530(c)	\$160,212
Total Costs					\$162,830
					\$189,014
5. Fixed Fee:					
7.5% of total costs (claimed rate)					14,176
total not accepted					<u>\$203,190</u>

Schedule I
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Explanatory Notes:

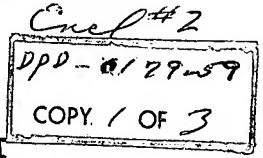
(A) Rate Claimed - 100%

(B) Rate Claimed - 150%

(C) Total G&A claimed @ 10% rate \$403,496
Less: Questioned above \$2,618
Questioned in Schedule III 348 2,966
Balance - G&A claimed on approved costs \$400,530

(D) If the items questioned in Schedule III are restored in negotiations, then the amount shown as approved base should be increased, thus increasing the costs questioned because of this rate difference.

Schedule II



Itek Corporation
Boston, Mass.
Subcontract Proposal to Prime Contractor
Costs Not Accepted - Schedule II of Cost Proposal

	<u>Base</u>	<u>Acceptable</u>	<u>Amount</u>		<u>Difference</u>
		<u>Rate</u>	<u>Acceptable</u>	<u>Claimed</u>	
1. <u>G & A</u>	\$6,867	6%	\$ 412	\$ 687(A)	\$275
2. <u>Fixed Fee:</u>		7.5% of above total (claimed rate)			<u>20</u>
		Total not accepted			<u>\$295</u>

Explanatory Note:

(A) Rate claimed - 10%

Schedule III

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Itek Corporation
Boston, Mass.

Subcontract Proposal to Prime Contractor
Costs for Further Consideration - Schedule I of Cost Proposal

1. Travel - Field Service:

See Par. 8.a.(2) of Report comments	\$ 480
See Par. 8.a.(3) of Report comments	<u>3,000</u>
Sub total	\$3,480

2. G & A:

10% of sub-total (claimed rate)	<u>348</u>
Total costs	\$3,828

3. Fixed Fee:

7.5% of total costs (claimed rate)	<u>287</u>
Total for Further Consideration	<u>\$4,115</u>